By eschewing market-based prices for PSLs and instead accepting public financing for stadiums, teams are missing a remarkable revenue opportunity.

How the Packers Lost Out

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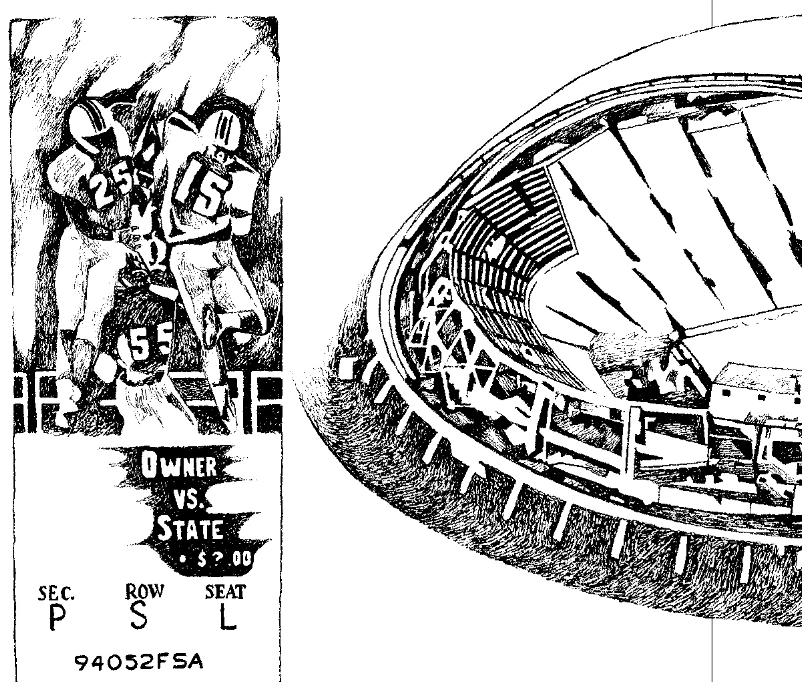
A few years ago, the Green Bay Packers decided to renovate their stadium in order to remain competitive in the NFL. They complained that Lambeau Field lacked many of the revenue-generating features that are staples of the newer stadiums, such as club seats, skyboxes, and ample concession stands.

Raising the money necessary to add such features proved to be tricky. Being a publicly owned corporation, the team lacked a deep-pocketed owner who could make the investment himself. The usual route for a professional sports team that wants to renovate or replace its current stadium is to ask the government to pay for the improvements. But in Green Bay, that option was problematic; a few years earlier, the state legislature narrowly voted to increase the sales tax in Milwaukee and nearby counties to pay for a new baseball stadium for the Milwaukee Brewers. The political fallout from that decision was significant, with the legislator who provided the deciding vote being recalled by an irate electorate. While the Packers argued that the team was an asset belonging to the entire state, the legislature was not going to risk incurring the wrath of voters again and would only contribute a small amount for infrastructure improvements.

Undeterred, the Packers chose to press the local government entity, Brown County, to impose an additional local sales tax of a half-percent to finance the remodeling of Lambeau Field contingent upon a countywide referendum. With the team coming off a string of successful seasons and the support of local political leaders, the Packers felt confident that they would win any referendum.



The team's lobbying efforts dwarfed that of its opponents. The Packers employed a slick public relations campaign, bringing back players from the glory days to appear in ads and meet with voters to impress upon them the need for their tax money. The Packer's campaign on the referendum presented a stark choice to the voters: If the referendum did not pass, they

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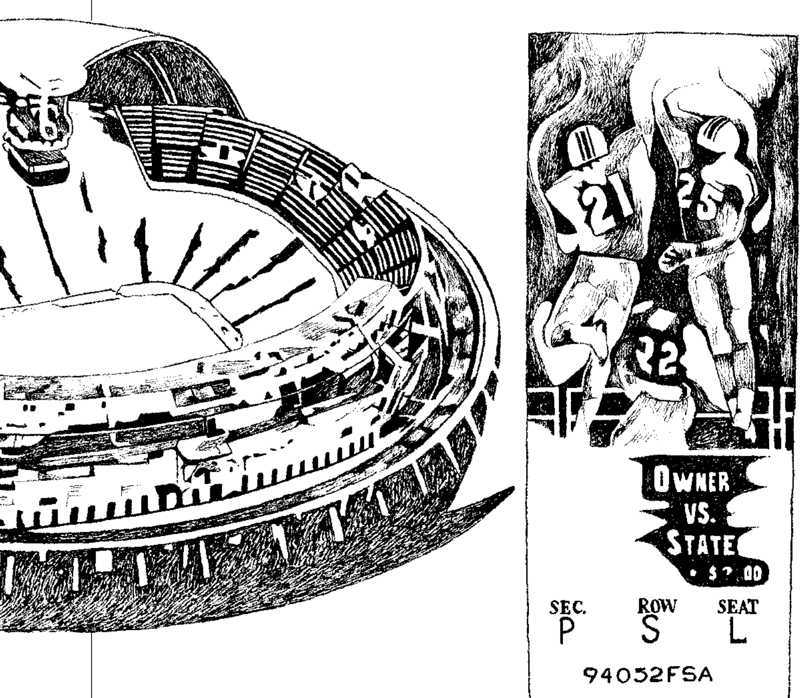
claimed, the team would either be forced to move or else declare bankruptcy within five years. The referendum narrowly passed.

PYRRHIC VICTORY?

The stark choice presented to voters was a lie: Because of its status as a publicly owned corporation that pays no dividend or capital gains, the team could not move anywhere. What is more, given the enthusiastic support the team receives across the entire state, it is difficult to conceive of where the Packers might move and generate more revenue, regardless of any sweetheart stadium deal they might receive from another community. And while the team's revenue was in the bottom half of the league when the referendum was passed, the ample amount of shared revenue in the league virtually guarantees an NFL team solvency regardless of the team's ancillary revenues. The projections offered by the team showing that it would soon be last in the league in revenue were pure sophistry.

The team could have raised sufficient revenue to cover the stadium renovation without resorting to government largesse. Instead, the Packers could have sold personal seat licenses (PSLs) – that is, the rights for fans to buy tickets for certain seats — at a price that reflected market demand, rather than for the pittance that the team actually charged. But the



Packers refused to sell PSLs at a price the market would bear, probably because of the risk-averse culture of professional sports as well as the willingness of governments to cough up money for stadiums.

The team should regret that it did not fully exploit the value of the PSLs. Thanks to the Internet and the increasing ease of online auctions, an entrepreneurial owner who fully exploits the value of PSLs will generate revenue dwarfing what the Packers received from their PSL sales. But, because they used the "traditional" stadium funding approach, the Packers likely will be in the same revenue situation in five years that they were in before the renovations took place, and not have the ability to rectify the situation.

MORGAN BALLARD

THE PSL ADVANTAGE

Personal seat licenses have been used by college and professional sports teams in some form for decades, but they became the "hot thing" in sports financing in the 1990s. A PSL is an example of what economists call "two-part pricing," which exists in many forms in today's economy (e.g., "shoppers clubs" in which customers pay a membership fee in order to shop in a specific store). In two-part pricing, customers are typically charged an entrance or participation fee to gain entrance into the market, and then they pay again for the right to buy whatever is in the market. Two-part pricing's primary advantage is that it makes it easier to price discriminate, or charge different people different prices for the same goods or services. In sporting events, the PSL is the participation fee, and teams discriminate by charging fans different prices depending on the location of their seats, how many seats they buy, and how many games in the season they are attending.

In the NFL, personal seat licenses have another crucial advantage: Money earned from PSL sales is exempt from the league's revenue-sharing formula. As it currently stands, teams must give their opponent 40 percent of the actual ticket revenues, but they can keep all of the revenue generated from the sale of PSLs. Thus, most teams that have used PSLs to finance new stadiums sell their season tickets below the market price, which increases the value of their PSLs and transfers revenue from shared ticket sales to the unshared PSL sales.

How the Packers lost While the Packers may be content with the $120 million raised from their sale of personal seat licenses, that revenue represents merely a fraction of what they could have collected had they fully exploited the true value of the PSLs.

The Packers made two mistakes when pricing their personal seat licenses. First, they failed to do any price discrimination at all: All PSLs went for $200 per seat per game, no exceptions. At a minimum, the team should have charged people different prices based on where their seats are, with those on the 50 yard line going for much more than those in the corner of the end zone. Nearly every other team that has sold PSLs has done as much; for instance, the Chicago Bears are charging $900 for their end zone seats and $10,000 for PSLs for the best seats.

The Packers could have come up with some canny pricing that would have dramatically increased revenue. For instance, thanks to the Packers' former practice of playing three games a year in Milwaukee, the team has two different sets of season tickets; the seven-game "Green" plan and the three-game "Gold" plan that was marketed to Milwaukee-area fans. The two plans enable a wider group of fans to bid on a season ticket plan, further stimulating demand. All baseball and basketball teams sell partial-season tickets, and they charge higher per-game prices for those who buy partial tickets. However, the Packers declined to do that, charging the Green ticket holders $1,400 and the Gold ticket holders $600.

Why the low PSL price? The Packers had a good reason for setting a below-market price for their PSLs. First, the team was undoubtedly afraid that a PSL price that appeared to "gouge" the season ticket holder would undermine public support for government subsidization of the Lambeau renovation. The politics of the referendum were tricky: While there are many fervent Packers fans in Brown County, a large number of them had no interest in having their tax money used to rebuild a stadium that they could never afford to enter in order to increase the salaries of the richest people in the area. Season ticket holders realized that if the ballot proposition were defeated, the value of their season ticket would fall appreciably — either the team would raise the PSL price or the stadium would not be remodeled and the team's performance (and the value of season tickets on the black market), likely would decline. Thus, keeping the PSL price low created an entire class of people with a vested financial stake in the referendum succeeding.

Another possible argument for setting a low price is that it represented the team's best estimate of its true value. Such a claim strains credulity: Season ticket holders routinely sell their entire slate of games to ticket brokers, racking up profits of anywhere between $500 and $2,000 a year. Anyone, even a non-fan, would pay more than $600 or $1,400 for an asset generating that much profit. It would not take much of a businessman to see that the price was well below demand.

Had the Packers truly been interested in maximizing their profit from the sale of PSLs, then the timing of the PSL sale could not have been better: Not only was the team coming off a string of successful seasons in the middle of a robust economy, but the explosive growth of the Internet and the development of auction software and websites offered the Packers a chance to reap unprecedented revenues by fully exploiting the value of the team and the personal seat license. A properly designed auction of the team's personal seat licenses could have raised over $1 billion.

THE MARKET PRICE OF A PSL

When remodeling is completed, Lambeau Field in Green Bay will hold about 69,000 seats, right around the NFL average. The team could easily fill a stadium twice that size; the waiting list for a season ticket was over 50,000 before the PSL sale, and relatively few people gave up their seats because of the sale.

How much would the market value a PSL be? It would depend upon the demand for tickets over the next few years, which in turn depends on the Packers' performance and a host of other factors. The value of the PSL would also be contingent upon the perception that the team would not build a new stadium in the near future and declare the PSLs obsolete. The future price of the game tickets matters, too. If the Packers decide to raise season ticket prices after the PSLs are sold, then the profits accruing to the PSL holders would disappear, as would their value.

Also, the degree of fungibility that comes with a PSL affects its value. If the owner is perfectly free to sell his PSL to whomever he wishes without interference from the team, its market value would be higher than if the team were to place a tax on each sale or demand that any PSLs not used by the owner be returned to the team. By placing minimal guarantees on the property rights of the PSL holders, the team could maximize its revenue from the sale of PSLs.

Finally, the value would be affected by economic conditions as well, such as the market interest rate and the rate of inflation. There is nothing the team can do about those, but all other financial assets are subject to those vagaries as well.

Of course, many factors that affect the value of a PSL can be controlled by the team itself. If the team wanted to maximize the amount of revenue it received from a sale of personal seat licenses, it could promise in writing to limit ticket price increases to the rate of inflation, that the owners would have full property rights to their PSLs and could buy and sell them at will, and the team would guarantee the PSL holders the right to buy tickets for a set amount of time, perhaps 15 to 20 years. In essence, the team would need to make the PSL as much of a pure economic asset as it possibly could, to the extent that people who have no interest whatsoever in ever seeing a game in Lambeau Field would nevertheless consider purchasing a PSL as an investment.

PSLs' value To calculate the potential value of a PSL, we use the Green Bay Packers as an example. We will assume initially that the profit from a ticket to all 10 games equals $400, a conservative estimate. If we also assume a long-run interest rate of 10 percent (also conservative; the higher the assumed interest rate, the lower the value of the PSL) and that the team will guarantee the PSL holder rights for 25 years, then the sale of PSLs would generate roughly $280 million, which is approximately the cost of the stadium renovation.

If we make less restrictive assumptions, it becomes clear that if the team were to price PSLs correctly and structure the sale optimally, then the amount of revenue generated from such a sale would be enormous. For instance, using a seven percent interest rate and an annual profit per ticket per game of $100 over the 25 years, the value of personal seat licenses is $850 million.

The Packers could even get cheeky and announce that they would henceforth sell their game tickets for $1 to PSL holders, thus allowing them to transfer revenue taxed by the league at 40 percent to their untaxed PSLs. If the NFL could not legally prevent that move, then we would need to double the above numbers, giving us $1.7 billion.

The team could potentially reap additional revenue depending upon how clever they are with subdividing the PSLs across the season, and how much they exploit the opportunities for ancillary revenues during such an auction. For instance, many fans would not be able to pay for their seats immediately, offering the team the opportunity to provide financing at a reasonable rate. The loan would be fully collateralized because the team could simply reclaim the seat if the bidder defaults.

And consider what could potentially occur during a 10-day auction for permanent tickets to a team like the Packers that has a mythic hold over a state with six million people, most of whom live within three hours of the stadium. The auction would undoubtedly be on the front page of every single newspaper in the state, and be the subject of nearly all conversations. In such an environment, bidding could diverge entirely from the economic value of a PSL and form an asset-price bubble, a not-uncommon occurrence in such markets.

Reason to win? One potential problem with a team receiving so much money up front is that it might dampen their incentives to put a good product on the field. After all, if their personal seat licenses are not up for sale for another 20 years, why should it matter to management if the team's performance is lacking? And, in turn, would fans' interest in bidding for PSLs decrease out of fear that management would field weaker teams?

There are two different ways to deal with that problem: First, the team should stagger the length of the PSLs, so that a certain proportion of the seats revert back to the team any given year to be sold again. Not only would that increase the ownership's incentive to put a good product on the field, but offering shorter PSLs would make the PSL market even more accessible to fans, by giving liquidity-constrained fans the ability to buy a short-term PSL.

A second way to deal with the disincentive problem would be to create a futures market in seat licenses. Teams would be obligated to hold a position in the market so that they profit from an increase in the value of PSLs. While a futures market may sound like a ridiculously complex way to deal with what is essentially the right to see a football game, some form of a future market for PSLs would eventually develop regardless of whether an individual team formally constructs the market.

AN END TO GOVERNMENT LARGESSE?

In the race to grow revenue, a majority of major league sports teams have moved into new or remodeled stadiums in the past decade, nearly all of which were financed in part or in whole by government entities. Virtually all economists recognize the folly of such an exercise. A major league sports team creates few new jobs in a city; the vaunted "multiplier effect" that says $1 spent on a sports arena circulates in an economy to create $8 or $9 in new spending is little more than sophistry. Even if it were the case that a sports team created lots of ancillary jobs, money spent on a new stadium for a team is not creating any new jobs: Stadium construction is a zero-sum game in that regard, merely keeping jobs in place or stealing them from another locale. The beauty of personal seat licenses is that it magnifies the futility of such government spending; with this alternative revenue source, government stadium subsidies become nothing more than transfers from taxpayers to team owners and season ticket holders.

Preventing states from engaging in pointless bidding wars to keep teams (or other businesses) from moving will doubtless receive more attention in the near future, as large and stubborn state budget deficits expose the folly of the years of profligate spending in the 1990s. In the past, individual states have entered into compacts to attempt to prevent their governments from spending to bring jobs into their jurisdiction. The Great Lake States attempted such a covenant in the late 1980s, which lasted only until then-Gov. George Voinovich (R-Ohio) faced a difficult re-election and abandoned the agreement out of political expediency.

Such cartels will always fail; states cannot enter into binding agreements to limit spending on corporate largess, and even a smaller cartel like the one involving the handful of Great Lake States is difficult to govern and maintain without the help of the law.

The only way to permanently keep states from using tax dollars to attract sports teams or corporations is to pass a federal law prohibiting such behavior. A sensible proposal comes from Melvin Burstein and Arthur Rolnick of the Minneapolis Federal Reserve Bank, who call on Congress to use its power under the Commerce Clause of the Constitution to "prevent states from using subsidies and preferential taxes to attract and retain businesses." To cover the subsidies of professional sports teams, which normally play in arenas and stadiums owned by the government, a separate clause would need to be written mandating that municipalities either sell off such stadiums or charge teams a rental price that reflects the true market cost.

HAVE THE PACKERS LOCKED IN MEDIOCRITY?

Jerry Jones, owner of the Dallas Cowboys, has been pushing state officials in Texas for government help to build a new stadium for his team. If Jones, instead, were to institute a PSL auction like we have described, he likely would generate a billion dollars of revenue from fans of "America's Team." That would be enough to build a new stadium with the features he desires and would give him a few hundred million dollars to buy better players. In the wake of such a move, every team in the league would institute similar auctions and generate similar revenues.

That would leave the Packers, with their current PSL scheme, out in the cold. And this time there would be little they can do about it; local and state governments are unlikely to offer them any more subsidies and the publicly held team would be unable to move to another city that would. The Packers could try to buy back their current PSLs and then auction them off in the manner we have described, but the buyback may be legally impossible. With other teams improving their stadiums and players with money generated from PSL auctions, the Packers could again fall into mediocrity.

Stadium of stockholders The sky-high price of PSLs may be decried by many for pushing the game beyond the pocketbooks of the middle class, but that happened a long time ago. However, market-priced PSLs will actually be beneficial for the fans in two different ways: First, the PSL holders will have not just a fan allegiance but also a fiduciary interest in the team; the better the team does, the more the PSL is worth. More than 60,000 investors seeing the value of their asset fall can create quite a bit of pressure on a team board of directors to turn things around, especially if they all happen to get together 10 times a year. The publicly held Packers have "stockholders" of a sort, although the stock pays no dividend. Were PSLs to become a fungible economic asset, the power of the license holders could trump that of the stockholders, making for interesting corporate-governance issues.

PSLs will benefit the fans who do not have season tickets by not using the government to extort money from them to pay for the new stadiums. Once any team attempts to auction personal seat licenses and generates revenue anywhere near what basic economic analysis would predict, it will expose the lie that public financing is needed for a new stadium. The idea that a professional sports stadium is some "public good" is ludicrous, and serves as an example of policymakers and politicians using rhetorical obfuscation to force a special interest's project upon the masses. R